Supreme Court, U.S.
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No. 00-1393

IN THE

Supreme Court of the United States

CO-STEEL RARITAN,

Petitioner,

v.

NEW JERSEY BOARD OF PUBLIC UTILITIES,

Respondent.

On Petition for Writ of Certiorari
To the Supreme Court of the State of New Jersey

BRIEF OF RESPONDENT NEW JERSEY BOARD OF PUBLIC UTILITIES IN OPPOSITION

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COUNTER-STATEMENT OF THE CASE

A. Procedural History

The New Jersey Board of Public Utilities ("BPU") is an agency within the Executive Branch of the State Government which has been vested by the State Legislature with general jurisdiction and control over all public utilities in New Jersey. *N.J.S.A.* 48:2-1 and 2-13. This case arises out of the BPU's August 24, 1999 Final Decision and Order ("Final Order") (165a)[1], resolving Public Service Electric and Gas Company's ("PSE&G") rate unbundling, stranded costs and restructuring filings, and a related September 17, 1999 Bondable Stranded Costs Rate Order ("BSCRO")(111a), allowing PSE&G to issue bonds to refinance certain of its stranded costs. The Orders were issued pursuant to the Electric Discount and Energy Competition Act of 1999, *N.J.S.A.* 48:3-49 *et seq.* ("EDECA").

Petitioner Co-Steel Raritan ("Co-Steel") and two other parties, the Division of the Ratepayer Advocate ("RA") and the New Jersey Business Users ("NJBUS"), appealed from the BPU's Orders. On April 13, 2000, the Superior Court of New Jersey, Appellate Division ("NJAD"), the State's intermediate appellate court, issued a detailed Order unanimously affirming the BPU's Final Order and BSCRO, and rejecting Co-Steel's arguments, which focused primarily on the narrow issue of the impact of the BPU's decision on Co-Steel's already-discounted Special Contract rates, as well as the more general substantive and due process arguments raised by the RA and NJBUS. ("NJAD Order")(14a).

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[1] "_a" denotes the appendix filed by Co-Steel with its petition to this Court. "_sa" denotes the supplemental appendix filed by Co-Steel.

Thereafter, Co-Steel filed a notice of appeal with the State's highest appellate court, the New Jersey Supreme Court ("NJSC"), purportedly pursuant to *R.* 2:2-1(a)(1), which provides for an appeal as of right in cases involving a "substantial question arising under the Constitution of the United States or this State." By Order dated July 14, 2000, the NJSC ruled that the appeal "does not raise a substantial constitutional question in accordance with *R.* 2:2-1(a)(1) and the case law interpreting that provision." (11a). The NJSC on its own motion, however, decided to review Co-Steel's submission under the standards applicable to a petition for certification and granted certification, limited to one statutory interpretation issue,[2] while denying certification as to all other issues raised, "including claims of impairment of contract." *Id.* The NJSC also granted petitions for certification filed by the RA and NJBUS. (13a).

After supplemental briefing and oral argument, the NJSC, recognizing the need for expedited resolution of the appeals, issued an Order on December 6, 2000, affirming the NJAD's Order by a 4-1 vote. (1a).[3] The Order stated that the opinions of the Court would be filed "in due course." *Id.*

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[2] The issue was whether the initial 5% rate reduction required by *N.J.S.A.*48:3-52(d)(2) of EDECA on August 1, 1999, should be measured relative to 1999 or 1997 rates.

[3] The Final Order provided that customers would receive an additional 2% rate reduction after PSE&G issued bonds to refinance its stranded costs at a lower interest rate. PSE&G was unable to issue such bonds while the appeals were pending, which, in turn, delayed the additional rate reduction. Shortly after the NJSC issued its December 6, 2000 Order, the bonds were sold and the rate reduction was implemented.

On March 6, 2001, Co-Steel filed a Petition for a Writ of Certiorari. The BPU sought and received permission to extend the time for filing its responding brief until after the opinions of the NJSC were issued. On May 18, 2001, the NJSC issued its opinions in this matter. (1sa). The time for filing responding briefs was later extended until July 9, 2001.

B. Background and Overview of the BPU's Final Order

As summarized in the NJAD's Order, the BPU's Final Order was the result of a five-year process to restructure the electric industry in New Jersey to facilitate the emergence of a competitive electric supply marketplace so as to lower costs and rates and improve the quality and choices of service for all customers. (20a-29a). Specifically, in March 1995, the New Jersey Energy Master Plan Committee issued a report ("EMP Report") outlining a general policy framework for a transition from power supply monopolies to competitive markets and directed the BPU to investigate changes to the structure of the electric industry as a means of lowering the cost of electricity in the State. The EMP Report also recommended several interim measures, including the enactment of transitional legislation, to help retain "at risk" customers during the transition to full competition. One such "at risk" customer was Co-Steel Raritan, which, at the time, was threatening to close its in-State steel mini-mill and shift production to a state with lower energy costs. As described below, in 1995 the BPU acted under its existing authority to retain Co-Steel as a customer of PSE&G by approving a ten-year Special Contract at sharply discounted rates. (31a-32a).

In response to the directive of the EMP Report, the BPU began a proceeding to investigate changes to the electric industry in New Jersey, which included public hearings and

comments, negotiations among representatives of the various affected stakeholders, and the release for comments of a draft report. On April 30, 1997, the BPU issued an Order adopting a Final Report entitled "Restructuring the Electric Power Industry in New Jersey: Findings and Recommendations" ("Final Report"), containing its findings and recommendations to introduce competition into the State's retail electric marketplace. (24a). The Final Report noted the need for enabling legislation "to provide the foundation and necessary legal authority for the changes recommended." *Id.*

Anticipating that competition could begin by late 1998, the BPU directed each of the State's four electric utilities to submit rate unbundling, stranded costs and restructuring filings by July 1997. The rate unbundling filings involve the manner in which the single per kilowatt-hour ("kWh") charge would be separated into its component parts (generation, transmission, distribution, etc.); the stranded costs filings relate to the quantification and rate treatment of the utilities' above-market, *i.e,* stranded, costs that would have been recoverable had they continued as regulated monopolies; and the restructuring filings relate to the corporate reorganization of the utilities in a competitive environment, including the possible divestiture or transfer of generating assets.

PSE&G's filings, submitted in July 1997, received intense administrative scrutiny. The rate unbundling and stranded costs filings were the subject of 20 days of evidentiary hearings before an Administrative Law Judge ("ALJ"). An additional 20 days of hearings were held before the BPU on the restructuring filing. More than 40 parties participated and over 20 parties, including Co-Steel, filed testimony analyzing and contesting various elements of PSE&G's proposals. In addition, the BPU hired an

independent auditing firm ("ICF") to audit PSE&G's filings. Extensive initial and reply briefs were filed. (175a-180a).

A detailed 101-page Initial Decision ("ID") was issued by the ALJ in August 1998 on the rate unbundling and stranded costs issues, the key elements of which are summarized in the Final Order (183a-199a). The ALJ made specific findings on the numerous individual disputed issues, but did not quantify the resulting total recovery-eligible stranded costs dollar amount, suggesting instead that the parties meet to quantify the results of his recommendations. When the parties were unable to agree on a quantification, BPU Staff ("Staff") asked ICF, the independent auditor hired by the BPU, to quantify the ALJ's findings. In November 1998, Staff sent a letter to the BPU and all parties enclosing ICF's calculations and supporting workpapers, which detailed three different values for the ALJ's findings on net-of-tax stranded costs, depending on what assumptions are used for the rate of inflation. (54a). Staff's cover letter indicated that the submission "represents the best interpretation and quantification of the ALJ's Initial Decision" by ICF, but noted that the quantification "does not necessarily represent the position of the BPU Staff." (54a-55a). No party responded to Staff's letter or raised any issue with any aspect of ICF's calculations. Exceptions and reply exceptions were filed to the ID. (200a-208a).

While the administrative review of PSE&G's filing was proceeding, restructuring legislation was being developed. In enacting EDECA on February 9, 1999, the Legislature determined that the traditional retail monopoly for electric power generation which electric public utilities have held in New Jersey for over 80 years should be eliminated, and all consumers shall be given the opportunity to access the competitive market and select an electric power supplier of

their choice by August 1, 1999. *N.J.S.A.* 48:3-50(b)(3). While New Jersey's move towards competitive retail power markets in many ways paralleled regional and national developments, EDECA provides a unique and distinct framework for the restructuring of New Jersey's electric utilities, notably, by requiring that substantial rate reductions be implemented and sustained over a four-year transition period, while simultaneously allowing electric utilities an opportunity to recover their stranded generation costs, and by pro-actively encouraging the development of a competitive energy supply market by immediately opening 100% of the retail market to full competition and providing for so-called "shopping credits" to stimulate competition.

EDECA establishes the framework and time schedule for retail electric competition in New Jersey. It mandates a 5% rate reduction by August 1, 1999, the start date for retail competition, and a 10% reduction from 1997 rates by August 1, 2002, to be sustained through July 31, 2003. *N.J.S.A.* 48:3-52. EDECA provides electric utilities the opportunity to recover eligible stranded costs, as determined by the BPU, through a limited-duration, nonbypassable market transition charge ("MTC"), *N.J.S.A.* 48:3-61, and to refinance certain eligible stranded costs, as determined by the BPU, through the issuance of asset-backed securities, to mitigate the rate impact of stranded cost recovery. *N.J.S.A.* 48:3-62. EDECA also permits utilities to recover the costs of certain approved social programs, conservation and environmental programs, as well as nuclear decommissioning and consumer education costs, through a nonbypassable societal benefits charge ("SBC"). *N.J.S.A.* 48:3-60. Unlike the case in some states, EDECA does not mandate divestiture, but permits utilities to divest their generation assets to third parties or to transfer them to a non-regulated affiliate, subject to a finding by the

BPU that certain conditions are met. *N.J.S.A.* 48:3-59. Significantly however, while EDECA sets forth clear policy directives and timetables for implementing retail choice and provides guidelines and parameters for the BPU to follow, it leaves many implementation decisions to the BPU's technical expertise in adopting individual rate unbundling, stranded cost recovery and restructuring plans for each utility.

Shortly after EDECA's enactment, the BPU set a schedule to render its decisions for each electric utility prior to the August 1, 1999 statutory deadline. The BPU encouraged the parties to attempt to negotiate settlements. While no unanimous settlement was reached in the PSE&G case, discussions among the parties led to the submission of two alternative non-unanimous settlement proposals, the first sponsored by PSE&G and seven other parties ("Stipulation I"); the second sponsored by the RA and five other parties ("Stipulation II"). (28a). Co-Steel was not a signatory party to either proposal. All parties were given the opportunity to submit written comments to the BPU on both proposals, and extensive comments and reply comments were filed by 20 parties. (243a-295a). Co-Steel filed comments limited to the issue of how Stipulation I would impact its Special Contract rates. (273a-275a).

On March 8, 1999, the Mid-Atlantic Power Supply Association moved to reopen and supplement the record in the PSE&G unbundling and stranded costs proceedings in light of EDECA and the settlement proposals. The RA and NJBUS supported the motion and PSE&G opposed it. Co-Steel took no position on the motion. By Order dated March 25, 1999, and again in its Final Order, the BPU rejected arguments that the record should be reopened for additional hearings, finding that there was ample evidence in the record for a decision and

that the proceedings had been conducted in contemplation of anticipated restructuring legislation. (28a; 300a). On this issue, the Final Order cites *N.J.S.A.* 48:3-98, which allows the BPU to rely upon filings submitted and proceedings conducted prior to, and in anticipation of, EDECA's effective date, provided "the board shall take such actions as may be necessary, if any, to ensure that the requirements of [EDECA] are met in all regulatory actions which were commenced prior to its enactment." (46a). The BPU found that this requirement of EDECA had been met and that the filings submitted and the proceedings prior to EDECA's effective date were thorough and complete and satisfied its requirements. (298a).

The BPU considered the PSE&G matter at its April 20, 1999 public agenda meeting. Finding Stipulation I to be more financially sound and consistent with EDECA's requirements than Stipulation II, and after careful consideration of the record, the BPU issued a Summary Order on April 21, 1999 (356a-364a), and a detailed Final Decision and Order on August 24, 1999 (165a-355a), incorporating, as a fair resolution of the proceedings, the framework and major elements of Stipulation I, with significant modifications to key provisions, including those related to rate reductions, stranded costs and the transfer of assets. The BPU's modifications reflect consideration of the concerns raised in the comments and by the proponents of Stipulation II. (300a-301a).

The 126-page Final Order contains detailed interrelated findings, supported by the vast record. The findings include: the establishment of a four-step rate reduction to be phased in and sustained during the transition period; a determination as to certain allowable sources of funding for the rate reductions; approval for the limited use of deferred accounting during the transition period; the establishment of shopping credits; the

valuation of PSE&G's generating assets and the determination of its recovery-eligible stranded costs based on the ALJ's recommendations as quantified by ICF (using the middle of ICF's three inflation rate scenarios); approval for PSE&G to transfer its generating assets to an unregulated affiliate at a determined price, subject to certain terms and conditions; a determination as to the level of stranded costs eligible for securitization; the establishment of nonbypassable market transition and societal benefits charges; the establishment of unbundled rates for the various rate classes; and findings as to how the rate reductions and nonbypassable charges would be applied to Co-Steel's Special Contract rates. (297a-355a).

Subsequently, on September 17, 1999, the BPU issued its BSCRO, allowing PSE&G to refinance or securitize certain of its stranded costs, subject to certain terms and conditions, and establishing a nonbypassable transition bond charge ("TBC") to reflect the rate impact of securitization. (111a). A motion for reconsideration filed by Co-Steel was denied by BPU Order dated October 19, 1999. (94a-110a).

C. Issues Relevant to Co-Steel's Petition

Co-Steel owns and operates a steel mini-mill in PSE&G's service territory in New Jersey. Prior to 1995, Co-Steel was served under PSE&G's High Tension Service ("HTS") Tariff. In late 1994, after Co-Steel threatened, absent significant relief from its high energy costs, to close its New Jersey facility and to move its production to a state with lower energy costs, Co-Steel and PSE&G negotiated a ten-year service agreement ("Special Contract"). The agreement provides that Co-Steel will remain in New Jersey and make capital improvements to its facility in exchange for receiving special discounted pricing during a ten-year term. The

agreement is silent as to what will occur after its expiration (32a), but includes a provision that it is "subject to present and future local, state and federal laws and to the regulations or orders of any local, state or federal regulatory authority having jurisdiction over the matters set forth herein..." ("Paragraph 9"). (34a). The agreement also provides that taxes, assessments, or other charges incurred by PSE&G in connection with the service provided, which were not applicable at the time of entering into the agreement, shall be passed through to Co-Steel. ("Paragraph 7"). *Id.* A stipulation modifying elements of the agreement was signed by PSE&G, Co-Steel, Staff and the RA in July 1995 and was approved by BPU Order dated November 17, 1995. (32a).

Under the approved Special Contract, electric service to Co-Steel is priced in two blocks: the first 13 million kWh ("Block 1"), about one-third of its monthly usage, continues to be billed "at prices, terms and conditions identical to PSE&G's then-effective Rate Schedule High Tension Service (HTS)," that is, at whatever the HTS tariff rate is at a particular time; charges on the remaining two-thirds of its usage are billed at a discounted rate ("Block 2 Discounted Rate"), pursuant to a newly created Experimental Hourly Energy Pricing Tariff ("EHEP"), based upon the wholesale hourly marginal energy price on the PJM power pool system serving Pennsylvania, New Jersey and Maryland. *Id.*[4]

The Special Contract reduced Co-Steel's annual electric bill by approximately 25% relative to the HTS tariff rates, from approximately $24 million to $18 million. (33a). In

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[4] Co-Steel is the only customer ever served under the EHEP Tariff. Approximately 200 large volume industrial customers take electric service under PSE&G's HTS Tariff.

addition, with the approval of the New Jersey Department of Treasury, Co-Steel received a discounted tax rate on energy purchased under the Special Contract. *Id.*

In the case before the BPU, Co-Steel argued that its Special Contract precludes the imposition of stranded cost charges either during or after the contract term. In its Final Order, the BPU determined that under *N.J.S.A.* 48:3-60, 61, and 67, HTS customers, along with all other electric public utility customers (except onsite generator customers, *N.J.S.A.* 48:3-77), were subject to nonbypassable stranded cost and societal benefits charges (MTC, TBC and SBC). At the same time, even while paying these charges, HTS customers would see overall rate reductions totaling 13.9% by August 1, 2002, which reductions were partly due to securitization of stranded costs. (33a). The BPU ruled that Co-Steel's Block 1 rate would reflect both the stranded cost charges and the rate reductions applicable to all HTS customers. Additionally, the BPU ruled that Co-Steel's Block 2 Discounted Rate, established pursuant to the Special Contract, would be unaffected by the BPU's Orders for the remainder of the term of the contract. Thus, the BPU did not modify the Special Contract, it simply enforced the contract as written; Co-Steel's Block 1 rate matches the current HTS tariff rates, as provided for in the Special Contract, and its Block 2 Discounted Rate remains unchanged for the duration of the ten-year agreement. (333a-334a).

The BPU also rejected Co-Steel's arguments that it should be exempt from any stranded costs charges after the expiration of the Special Contract. The BPU noted that after the Special Contract expires, Co-Steel will be subject to the same obligations and have the same rights as all customers under applicable law, including the ability to shop for an alternate supplier. (334a).

In its motion for reconsideration to the BPU, Co-Steel argued that the BPU's application of EDECA to Co-Steel's Special Contract rates violated the constitutional prohibition against impairing the obligation of contracts. (96a). Co-Steel also raised several alternative arguments, should the BPU maintain its position on the applicability of stranded cost charges to the Block 1 rates. (96a-97a). Among these was an argument that the statutory rate reductions should apply to both blocks of its Special Contract. Specifically, Co-Steel argued that EDECA mandates that rates for each customer class be reduced, and that its Block 2 discounted rates under the discounted EHEP tariff should be deemed a separate customer class for the purpose of rate reductions.

In response, PSE&G argued that Co-Steel cannot claim that EDECA supersedes the Special Contract to provide rate reductions while at the same time arguing that EDECA cannot supersede the Special Contract and allow for the imposition of stranded cost charges. PSE&G also cited to EHEP Tariff Page 85 which provides that "service under this rate schedule is available on an individual contract basis," and that "customer's cost of energy will vary hourly", with changes in "marginal energy cost" and that "all other terms of the service are described by the contract." (102a).

On reconsideration, the BPU reaffirmed its decision to apply the statutory charges and rate reductions to Co-Steel's Block 1 rates. The BPU also rejected all of Co-Steel's alternative arguments, including that the statutory rate reduction should be applied to Block 2 rates as well, finding that "it is much more reasonable to interpret the limited reference to 'customer class' set forth at [*N.J.S.A.* 48:3-52(d)] to mean customers served under fixed tariffs, not customers that have made separate arrangements to receive service at heavily discounted rates." (108a).

On appeal to the NJAD, Co-Steel argued that the BPU's Final Order constitutes an unconstitutional impairment of its Special Contract because it imposes unanticipated legislatively mandated stranded cost charges on Co-Steel's power usage both during and after the contract period. Co-Steel again raised several alternative arguments should its main contract impairment contention fail, including that the statutory rate reductions should apply to both blocks of its Special Contract.

The NJAD rejected all of Co-Steel's arguments. After discussing the federal and state constitutional provisions prohibiting the impairment of contracts, the relevant case law and the three-pronged test applied by federal and state courts to determine whether a contract has been unconstitutionally impaired, and after considering the facts and arguments in the instant case, the NJAD found that "[t]he BPU's decision was grounded solidly on holding the parties to the terms of Co-Steel's contract with PSE&G." (30a-38a). The NJAD further found that the legislatively mandated charges "are covered under the plain language of paragraph seven." (35a). The NJAD concluded that Co-Steel's contract had not been substantially impaired by the BPU's Orders implementing EDECA, but even if Co-Steel could satisfy this first prong of the test, it fails the second and third prongs, because there is a legitimate purpose behind the collection of stranded costs by utilities and the legislative policy to provide for a smooth transition from a regulated to a competitive power supply marketplace, while maintaining the financial integrity of the electric utility through the transition to competition. *Id.*

As to Co-Steel's liability for statutorily mandated stranded costs charges after the expiration of the Special Contract, the NJAD found that the Special Contract does not call for any special post-contract treatment, and that it is reasonable that Co-Steel bear its share of the stranded cost

charges that are an integral part of the deregulation scheme. (36a). The NJAD noted that when the contract expires, and if Co-Steel remains in New Jersey, it may also receive benefits from competition among energy suppliers. *Id.*

The NJAD also rejected Co-Steel's alternate argument that the statutory rate reductions should apply to both blocks of its usage. Fundamentally, the NJAD found that the BPU's determination to enforce the contract as written was a valid basis for the BPU's decision. (38a). Additionally, the NJAD upheld the BPU's determination that while Co-Steel had previously been given a special discounted rate, which literally put it into a class by itself, it should not be considered as a separate "customer class" under *N.J.S.A.* 48:3-52(d), for the purpose of receiving an additional rate decrease on top of its already heavily discounted rate. *Id.* The NJAD noted that the interpretation of "customer class" announced by the BPU, the administrative agency charged with enforcement of EDECA, should be given great weight by the court. *Id.*

As noted above, the State's highest appellate court declined to hear Co-Steel's arguments regarding alleged impairment of contract and denial of equal protection, finding that "the appeal does not raise a substantial constitutional question" warranting that court's review. (11a).

As to the alleged due process violations raised herein by Co-Steel, these issues were not raised by Co-Steel before either State appellate court. (Petition, footnote 42). They were, however, raised by other parties, and were carefully considered and decisively rejected by both the unanimous NJAD Order and the NJSC Majority Opinion. (20a; 42a-61a; 16sa). The NJAD concluded that, while the administrative proceedings leading up to the BPU's Orders were "unusual"

in a number of ways, due in very substantial part to the short time period in which EDECA mandated the onset of retail competition and rate reductions, all parties had ample opportunity to be heard on all aspects of all decisions and there was no denial of due process or fundamental unfairness. (20a; 61a). The NJAD "unhesitatingly conclude[d]" that the parties were provided with the essential requirements of due process throughout the hearings, comment periods and settlement negotiations, and that none of the alleged procedural irregularities rose to the level of a denial of constitutional due process or of State law. (61a). In particular, the NJAD found that the BPU did not err in declining to reopen the record for additional hearings after the passage of FDECA and/or after allegedly new issues were raised in Stipulation I, finding that the parties had notice and opportunity to be heard on all issues raised therein, including the asset transfer, and that the essential requirements of due process were met. (42a-52a). The NJAD further found that the BPU's reliance on the independent auditor's report to quantify the ALJ's findings "was not a procedural irregularity sufficient to deny the RA due process." (56a).

The State's highest appellate court, with one justice partially dissenting, affirmed the NJAD's Order in its entirety. (1sa). In affirming the NJAD's Order with respect to challenges regarding the BPU's reliance on the auditor's quantification of the ALJ's findings, the NJSC Majority Opinion found that the BPU's Final Order reflects findings "that are supported by the record and consistent with EDECA." (15sa). In determining that the BPU's decision on stranded costs and asset valuation should not be set aside, the NJSC Majority Opinion concluded:

The BPU's valuation of PSE&G's generation facilities

and its stranded costs were based on years of fact finding and extensive quasi-judicial and quasi-legislative proceedings. The parties participated fully and vigorously at all stages. We find no procedural infirmity that would compel us to remand at this juncture for additional hearings on those matters.

[16sa].

ARGUMENT

THE WRIT SHOULD BE DENIED SINCE PETITIONER HAS FAILED TO DEMONSTRATE A FEDERAL QUESTION OF PUBLIC IMPORTANCE, OR A CONFLICT WITH ANY DECISIONS OF THIS COURT OR ANY OTHER COURT; MOREOVER, THE ISSUES RAISED IN THE PETITION HAVE ALREADY BEEN REVIEWED AND PROPERLY REJECTED BY THE STATE APPELLATE COURTS

The writ sought herein should be denied because petitioner has failed to demonstrate a federal question of public importance and, in fact, concedes that "this case does not present a case in conflict with decisions of the courts below, nor a conflict among federal courts." (Petition at 16).

Notwithstanding Co-Steel's assertion that this is an "important case" (Petition at 16), at its essence, Co-Steel's petition involves a very narrow issue of limited applicability: whether the BPU properly applied the provisions of a 1999 State electric restructuring statute, which provides for rate reductions and for the assessment of certain charges to

customers, to the unique circumstances of one particular customer, who has been receiving the benefit of highly discounted rates through a one-of-a-kind, ten-year Special Contract, approved in 1995. This issue turns on its own facts and does not affect any customer other than Co-Steel, except to the extent that if Co-Steel is not assessed its fair share of the statutorily-authorized charges, the shortfall would have to be made up by other utility customers.

The issues raised in Co-Steel's petition have already been carefully considered and decisively rejected by the New Jersey appellate courts. In affirming the BPU's Final Order, the State intermediate court properly concluded that the BPU's decision with respect to Co-Steel's rates was consistent with and represented a reasonable application of the State statute, which did not substantially impair Co-Steel's pre-existing contract nor violate the Contracts Clause or deprive Co-Steel of its lawful rights. (29a-38a). In dismissing Co-Steel's appeal on this issue, the State's highest court correctly found that the appeal does not raise a substantial question arising under the United States Constitution. (11a). Moreover, while the due process issues raised in the petition were not raised by Co-Steel on appeal below, the New Jersey courts carefully considered the due process arguments raised by two other parties and correctly concluded that the parties were provided with the essential requirements of due process and that none of the alleged procedural irregularities rose to the level of a denial of constitutional due process or a violation of State law. (61a; 16sa).

Accordingly, as will be argued herein, the writ should be denied.

A. *As the New Jersey courts have already found, the BPU's decision to apply the statutory rate reductions and stranded costs charges only to Co-Steel's HTS tariff portion of its Special Contract, and not to the already-discounted rate portion of the contract, does not impair the contract nor violate the Contracts Clause*

The United States Constitution, art. 1, sec. 10, provides that "[n]o State shall ... pass any ... Law impairing the Obligation of Contracts ...." Assessing the validity of a Contract Clause claim involves a three part analysis. Courts must consider whether the challenged action, in fact, has caused a substantial impairment of a contractual relationship. If the challenged action has, in fact, caused a substantial impairment of contract, then the second inquiry is whether the regulatory measure came into being for a significant and legitimate public purpose. If a legitimate public purpose has been established, the inquiry shifts to whether the adjustment of the rights and responsibilities of the contracting parties caused by the action is based upon reasonable conditions and is reasonably related to the public goal to be achieved based upon the existing conditions. *United States Trust Co. v. New Jersey,* 431 U.S. 1 (1977).

As a threshold matter, it therefore must be determined whether the challenging party has demonstrated that the state law or regulatory measure has caused a substantial impairment of a contractual relationship. *Energy Reserves Group, Inc. v. Kansas Power and Light Co.*, 459 U.S. 400, 411 (1983). In determining the extent of any impairment, courts are to consider "whether the industry the complaining party has entered has been regulated in the past." *Id.* One whose rights,

such as they are, are subject to state restriction, cannot remove them from the power of the state by making a contract about them. *Id.*, citing *Hudson Water Co. v. McCarter*, 209 U.S. 349, 357 (1908).

Even assuming a demonstration of a substantial impairment of a preexisting contractual obligation, a Contract Clause violation will not be found simply because the state law affects the rights and obligations created by the contract. The prohibition on impairment of contracts does not prevent the state from exercising such powers as are vested in it for the promotion of the common weal or are necessary for the general good of the public. *Allied Structural Steel Co. v. Spannaus,* 438 U.S. 234, 241 (1978).

As the courts below have already found, it is clear that the BPU's decisions in this matter are not violative of the Contracts Clause. As described above, the BPU in its Final Order determined that under EDECA, *N.J.S.A.* 48:3-60, 61, and 67, HTS tariff customers, along with all other customers, (except for onsite generator customers, *N.J.S.A.* 48:3-77), were subject to nonbypassable stranded cost charges (MTC, TBC and SBC). At the same time, these customers would also receive rate reductions totaling 13.9% by August 1, 2002, which reductions were, in part, due to securitization of the stranded costs. The BPU determined that Co-Steel's Block 1 rates, which under the terms of the Special Contract were to be priced at the prevailing HTS rate, would reflect both the stranded cost charges and the rate reductions applicable to all HTS customers. The BPU further determined that the Block 2 rates, which under the terms of the Special Contract were priced at a competitive market-based rate significantly lower than the HTS rate, would remain unchanged for the duration of the Special Contract.

Thus, the BPU did not impair Co-Steel's Special Contract; it simply enforced the contract as written. In fact, as a result of the BPU's Final Order, Co-Steel's rates have decreased from the rates in effect as of July 31, 1999, as a result of the rate reductions applied to its Block 1 rates.[5]

In the appeal below, the NJAD properly applied the applicable law to the specific facts of this case and correctly concluded that "Co-Steel's contract has not been substantially impaired." (35a). The NJAD found that "the BPU's decision was grounded solidly on holding the parties to the terms of Co-Steel's contract with PSE&G," and further noted that "Co-Steel appears to admit that during the term of the contract [EDECA] as applied by the BPU order, will not impair its contract, but will in fact enhance it." (38a; 33a).

As to Co-Steel's arguments that after the expiration of the Special Contract it will be subject to unanticipated stranded cost charges, the NJAD correctly found that Co-Steel's arguments were undermined by its failure to include contingencies for post-contract charges, even though it knew that electric restructuring was likely to occur during the term of the Special Contract. (34a). The NJAD also noted that the

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[5] Co-Steel's suggestion on page 19 of its petition that its rates during the contract term will be higher than originally bargained for is wrong; Co-Steel's contract provides for the inclusion of increases in "demand side management" charges on both its Block 1 and Block 2 rates, which charges were passed through to it in a prior April 1, 1998 Order of the BPU. (107a). Moreover, Co-Steel's claim, at page 9 of the petition, that future stranded cost charges will essentially equal or exceed its savings under the Special Contract, is based on its unsubstantiated and unverified estimate of such charges for a period some 10 years past the expiration of the Special Contract. During the term of the Special Contract, and during the period of the rate reductions mandated by EDECA, it is undisputed that its rates will decline.

express language of Paragraph 9 of the Special Contract (See, page 9-10, *supra*) suggests that "Co-Steel knew that its contractual rights were subject to alteration by state legislation," and thus "cannot have reasonably relied on the immutability of the agreement." (34a-35a). The NJAD also reasoned that the State Legislature had mandated that stranded cost charges be passed along to customers as a cost of service, and, as such, the charges were covered under the plain language of Paragraph 7 of the Special Contract (See, page 9, *supra*). (35a). The NJAD concluded that:

> Co-Steel appears to want a "double bite," the favorable contract rate and the advantages of competition, but none of the associated costs of deregulation. The equities do not favor Co-Steel under these circumstances. Their reliance was not so much detrimental as it was shrewd.
>
> [37a].

For all these reasons, the NJAD correctly found that Co-Steel's contract had not been substantially impaired. Moreover, the NJAD properly concluded that even if Co-Steel could satisfy this first prong of the test, it would fail the second and third prongs, noting that Co-Steel concedes that there is a legitimate purpose behind the collection of stranded costs by utilities, and recognizes EDECA's stated policy to provide for a smooth transition from a regulated to a competitive power supply market and to maintain the financial integrity of the electric public utility through the transition to competition. *N.J.S.A.* 48:3-50(a)(12) and (c) (4). (35a). As noted above, the State's highest appellate court declined to hear an appeal on this issue, finding that Co-Steel did not raise a substantial constitutional question. (11a).

The BPU respectfully submits that the decisions of New Jersey's appellate courts, affirming the BPU's application of EDECA to the unique circumstances of Co-Steel and rejecting Co-Steel's Contracts Clause arguments, are correct and well-reasoned and entirely consistent with applicable law. Accordingly, insofar as it is based on Contracts Clause arguments, the writ should be denied.

B. As the New Jersey courts have already found, the BPU's decision not to apply the statutory rate reductions and stranded costs charges to the Block 2 rates for the duration of the Special Contract does not violate the Equal Protection Clause

Co-Steel's "equal protection" argument is similarly plainly without merit. The Equal Protection Clause requires, that in defining a class subject to legislation, the distinctions that are drawn have "some relevance to the purpose for which the classification is made." *Baxstrom v. Herold*, 383 *U.S.* 107, 111. (1966). The BPU's application of EDECA to the unique circumstances of Co-Steel's Special Contract rates clearly has a rational basis related to the legislative intent.

*N.J.S.A.*48:3-52(d)(1) provides in pertinent part: "During a term to be fixed by the board, each electric public utility shall reduce its aggregate level of rates for each customer class, including any surcharges assessed pursuant to this act, ..." Relying on this provision, Co-Steel alternatively argues that since it takes service as a "class," albeit a special class of one, it is entitled to the rate reductions mandated by EDECA as to both Blocks 1 and 2.

This argument was rejected by the BPU based upon its interpretation of the new statutory provisions. Specifically, the BPU found that " it is much more reasonable to interpret the limited reference to 'customer class' set forth at [*N.J.S.A.* 48:3-52(d)(1)] to mean customers served under fixed tariffs, not customers that have made separate arrangements to receive service at heavily discounted rates." (108a).

The NJAD, in its review of the BPU's decisions, properly found that the interpretation of "customer class" announced by the BPU, the administrative agency charged with the enforcement of EDECA, was reasonable in light of Co-Steel's already-discounted Block 2 rate and should be given great weight by reviewing appellate courts. (38a). In so ruling, the NJAD relied upon well-settled State law regarding statutory interpretation by the implementing agency. *Id.*

While the NJSC Opinions did not address Co-Steel's contract issues directly, in affirming the NJAD's decision, the Majority Opinion noted that the case before the BPU implicates questions of statutory interpretation, and that under well-settled State case law, since the grant of authority to an administrative agency is to be liberally construed to enable the agency to accomplish the Legislature's goals, reviewing courts must defer to the agency's interpretation, provided it is not plainly unreasonable. (5sa-6sa).

Given the unique circumstances of the Special Contract with a heavily discounted Block 2 rate, together with the need to interpret a new statute in a fair and reasonable fashion, it is clear that the BPU acted within its discretionary authority when it determined that the statutory cost charges and rate reductions would apply only to those charges directly tied to the HTS rate and not to the negotiated Block 2 Discounted

Rate. The BPU, in essence, determined to leave the Special Contract as negotiated by the parties, since the Special Contract itself provided that Block 1 rates would be adjusted for changes in the HTS tariff. (106a; 32a).

It is important to note that the intent of EDECA is to lower the current high cost of energy and improve the quality and choice of service for all of the state's residential, business and institutional customers. *N.J.S.A.* 48:3-50(a)(1). To accomplish this, the Legislature determined that certain stranded costs needed to be assessed on all customers, subject to the regulatory discretion of the BPU, to pave the way for competition. Given the legislative intent in this regard, the BPU's determination to apply the rate reductions to Co-Steel's Block 1 HTS tariff rate only, and not to the Block 2 Discounted Rate, is a reasonable interpretation of EDECA. Because the HTS tariff Block 1 rate charged to all HTS customers reflects PSE&G's cost of providing service, including any stranded costs it may incur, it is consistent with the legislative intent that all stranded cost charges and statutory rate reductions under EDECA should apply. However, because Co-Steel's Block 2 Discounted Rate is based on a competitively priced marginal cost of power on the PJM system, the rate reductions and associated stranded cost charges should not apply. This position is well grounded because there is in fact no connection between the statutory rate reductions, with the associated stranded costs, and the Block 2 Discounted Rate. In other words, the Block 1 rates are based on an HTS tariff established to reflect PSE&G's costs, while the Block 2 Discounted Rates are already competitively priced PJM-based rates.[6] This is a fair and

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[6] The Block 2 Discounted Rate is based on the hourly marginal energy cost of the electric consumption (the PJM billing rate or successor rate) plus other adjustments for taxes, line losses and fuel adjustment charges.

reasonable result. In contrast, were the BPU to have adopted Co-Steel's argument on this issue and apply the rate reduction to Block 2, the Block 2 rates, which comprise two-thirds of Co-Steel's usage, would actually be priced below the wholesale marginal cost of energy to serve Co-Steel, clearly an unfair and unreasonable result that is contrary to the legislative intent to "afford fair treatment to all stakeholders during the transition [to full competition]." *N.J.S.A.* 48:3-50(a)(12).

As the NJAD aptly noted in this regard, Co-Steel appears to want a "double bite," the favorable contract rate and the statutory rate reductions on top of its already-discounted rate, but none of the associated costs of deregulation. (37a). In order to forestall Co-Steel's departure from the State and the attendant economic ramifications thereof, Co-Steel was singled out for special treatment in 1995, consistent with the State's Energy Master Plan Committee's recommendation that interim measures be undertaken to retain "at risk" customers. (See, page 3 *supra*). Co-Steel received the benefit of competitive electric rates well before EDECA brought the promise of competitive electric rates to PSE&G's other 200 large volume HTS customers in New Jersey. EDECA was enacted to bring the benefits of competition and lower electric rates to all of the State's customers. In view of the substantial discount in electric rates which Co-Steel has already received and will continue to receive under the Special Contract, and because two-thirds of its discounted rate is governed by precise terms associated with market based marginal cost pricing which predates EDECA and has nothing to do with PSE&G's operations or its need, in conformance with EDECA, to reduce rates by August 1, 2002, it was eminently reasonable for the BPU to limit the applicability of both the stranded cost charges and the statutory rate reductions to that portion of Co-Steel's usage which reflects

the cost of PSE&G's operations, that is, the Block 1 HTS tariff rate. Therefore, the BPU's determination of this issue represents a reasonable interpretation of the legislative intent and constitutes a sensible exercise of its discretion in interpreting a new statute. Accordingly, as to the "Equal Protection" arguments, the writ should also be denied.

C. As the New Jersey courts have already found, all parties were afforded adequate due process in the proceedings below

Notably, the federal due process issues alleged in the writ were not raised by the petitioner below. Significantly, there is no allegation that Co-Steel was precluded from presenting any of its evidence and arguments to the BPU at any stage of the proceedings before the BPU, including the litigation, comment and negotiations phases of the proceeding, or in its subsequent motion for reconsideration. Each and every one of Co-Steel's arguments was carefully considered by the BPU. Moreover, the BPU in its decisions carefully articulated the reasons why Co-Steel's arguments were rejected, consistent with applicable law and based on record evidence. As such, there is no credible basis for Co-Steel to now assert that it was denied due process.

Significantly, the State reviewing courts below considered and rejected procedural challenges to the BPU's decision by the RA and NJBUS, including that the decision violated federal and State due process protections, principles of fundamental fairness, the State's Administrative Procedure Act, the State restructuring statute and the BPU's regulations.

were "unusual" in a number of ways, due in very substantial part to the short time period in which EDECA mandated the onset of retail competition and rate reductions, "unhesitatingly conclude[d]" that the parties were provided with the essential requirements of due process throughout the hearings, comment periods and settlement negotiations, and that none of the alleged procedural irregularities rose to the level of a denial of constitutional due process or State law. (61a). Similarly, the State's highest court, affirming the intermediate appellate court's decision, found no procedural infirmities which would require a remand for additional hearings, finding that the BPU's valuation of PSE&G's generation facilities and its stranded costs determination "were based on years of fact-finding and extensive quasi-judicial and quasi-legislative proceedings" and that the parties "participated fully and vigorously at all stages." (23sa). Thus, there is no important federal due process issue here which requires this Court's review. Accordingly, the writ should be denied with respect to Co-Steel's belatedly-asserted due process issue.

CONCLUSION

For all the above reasons, the New Jersey Board of Public Utilities respectfully submits that Co-Steel Raritan's Petition for Writ of Certiorari should be denied.

Respectfully submitted,

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